

#### GENERAL INFORMATION

*The Community Reinvestment Act ("CRA") requires each federal financial supervisory agency to use its authority when examining financial institutions subject to its supervision to assess the institution's record of meeting the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with the safe and sound operation of the institution. Upon conclusion of such examination, the agency must prepare a written evaluation of the institution's record of meeting the credit needs of its community.*

*This document is an evaluation of the CRA performance of Montana State Bank, Plentywood, Montana, prepared by the Federal Reserve Bank of Minneapolis, the institution's supervisory agency, as of May 28, 1996. The agency rates the CRA performance of an institution consistent with the provisions set forth in Appendix A to 12 CFR Part 228.*

**INSTITUTION'S CRA RATING:** This institution is rated "Satisfactory."

The CRA evaluation revealed several factors that support rating the bank's CRA performance satisfactory. First, the bank's loan-to-deposit ratio is reasonable given the credit demands and demographics of its assessment area. Second, the bank has originated a majority of its loans to assessment area residents. Third, the bank actively extends loans to low- and moderate-income individuals and to small farms.

*The following table indicates the performance level of Montana State Bank, Plentywood, Montana, with respect to each of the five performance criteria.*

SMALL INSTITUTION ASSESSMENT CRITERIA	MONTANA STATE BANK PERFORMANCE LEVELS		
	Exceeds Standards for Satisfactory Performance	Meets Standards for Satisfactory Performance	Does Not Meet Standards for Satisfactory Performance
Loan-to-Deposit Ratio		X	
Lending in Assessment Area		X	
Lending to Borrowers of Different Incomes and to Businesses of Different Sizes	X		
Geographic Distribution of Loans		X	
Response to Complaints	The bank has not received any CRA complaints since the last evaluation.		

## **DESCRIPTION OF INSTITUTION**

Based on its size and financial condition, the bank is able to meet the credit needs of its assessment area effectively. This is the bank's first CRA evaluation since it became a state member bank. The bank's performance in meeting community credit needs at its previous CRA evaluation performed by the Office of the Comptroller of the Currency was satisfactory. The bank operates one full-service office and one automated teller machine ("ATM") in Plentywood, Montana. The ATM is a cash-dispensing machine, which is accessible 24 hours a day. The bank's main office and ATM, situated centrally within the assessment area, are located in a middle-income BNA. The bank has not opened or closed any offices since its inception.

According to its March 31, 1996, Report of Condition ("ROC"), the bank's assets totaled approximately \$38.6 million. The March 31, 1996, ROC indicates that the bank is primarily an agricultural lender; approximately 62% of its loan portfolio is composed of agricultural loans. The balance of the bank's loan portfolio is composed of 20% commercial, 10% consumer, 5% other, and 3% consumer real estate loans. The composition of the bank's loan portfolio reflects the level of demand for specific types of loans by members of the assessment area.

The bank offers a variety of loan products to fulfill the credit needs of residents and businesses within its assessment area. It extends consumer, residential real estate, mobile home, commercial, and agriculture loans. In addition to these conventional loan products, the bank offers and is willing to extend Farm Service Agency, Federal Housing Administration Title I, Small Business Administration, and federally guaranteed student loans. The bank also periodically refers applicants for residential real estate loans to a third-party creditor.

## **DESCRIPTION OF MONTANA STATE BANK'S ASSESSMENT AREA**

The bank has defined its assessment area as Sheridan County, Montana, which is located in the northeastern most corner of the state. The assessment area contains block numbering areas ("BNA") 9501, 9502, and 9503. There are no low-income BNAs in the assessment area. BNA 9503 is designated as moderate income. The remaining BNAs within the assessment area, 9501 and 9502, are classified as middle income.

The bank's assessment area is in Montana's northern region, known as Missouri River Country. The communities located within the assessment area include Plentywood, Raymond, Antelope, Westby, Coalridge, Dagmar, Outlook, Reserve, and Homestead, Montana. With only 4,732 residents, the assessment area is sparsely populated. According to 1990 U.S. Census data, Plentywood's population is 3,133, representing 66% of the assessment area's population. The bank's assessment area also includes the northeastern section of the Fort Peck Indian Reservation ("Reservation"). The Fort Peck Assiniboine & Sioux Tribe has approximately 11,000 members. Approximately 6,000 tribal members reside on the Reservation.

CRA divides income levels into four categories: low income, moderate income, middle income, and upper income. Because the bank's assessment area is not located in a metropolitan statistical area, the categorization of a borrower or BNA's income is determined relative to the statewide nonmetropolitan median family income. Pursuant to CRA's definitions, low-income individuals have incomes of less than 50% of the statewide nonmetropolitan median family income, while moderate-income individuals have incomes of at least 50% but less than 80% of this amount. The regulation defines middle-income individuals as persons with an income of at least 80% but less than 120% of the statewide nonmetropolitan median family income. Individuals with incomes of 120% or more of the statewide nonmetropolitan median family income are classified as upper-income persons. BNAs are classified using similar categories based on the level of the median family income in the geography. According to the 1995 updated census data, the statewide nonmetropolitan median family income in Montana is \$32,200.

According to the 1990 U.S. Census data, the assessment area's median family income is \$25,265, while its median household income is \$20,728. There are 1,353 families and 1,894 households in the assessment area. Approximately 11% of the families and 15% of the households residing in the assessment area have incomes below the poverty level. The distribution of family and household income for the assessment area is summarized in the following table.

ASSESSMENT AREA POPULATION DISTRIBUTION BY INCOME LEVEL				
Unit of Measure	Low Income	Moderate Income	Middle Income	Upper Income
Households Compared to Median Household Income	24%	19%	20%	37%
Families Compared to Median Family Income	21%	23%	24%	33%

Examiners contacted local government board members and a tribal government representative as part of the bank's CRA evaluation. Information from these contacts was used in evaluating the bank's CRA performance.

According to bank management and community contacts, the economy in the bank's assessment area remains strong and stable. The continued economic stability is attributed to the region's diversified agricultural industry. Cattle ranchers and grain farmers represent the primary local agriculture sectors. Since the agriculture prices in these two sectors tend to be countercyclical, the general economy rarely experiences periods of extreme highs or lows. The demand for credit by local ranchers and farmers is limited because farm operations are passed from one generation to the next.

The oil industry also has a significant presence in the bank's assessment area. In the 1980s, oil companies' successful drilling in the local area significantly raised the per capita income of local residents; in 1982, Sheridan County was one of the 50 wealthiest counties in the nation based on per capita income. Consequently, local residents increased their deposits at the local financial institutions. As a result of the increased wealth and cash assets of residents, local financial institutions experienced lower demand for credit. This situation is expected to continue as new drilling techniques are employed to locate more oil deposits in the area.

Plentywood is the assessment area's retail and government center and is the county seat of Sheridan County. Despite its small size, Plentywood is served by three financial institutions, making the market for financial services very competitive. Local residents and businesses also have access to credit from a number of other providers: credit unions in Medicine Lake and Scobey, Montana; a bank in Froid; and Farm Credit Services.

Assessment area residents are served by a regional hospital, which is one of

the primary local employers, and a nursing home; both institutions are located in Plentywood. Because of the county's sparse population, many local businesses are the sole provider of their respective services within the assessment area. Although local residents have access to grocery stores, convenience stores, restaurants, and service stations in Plentywood, they often travel 60 miles to Williston, North Dakota, for retail and medical services.

The region's commercial sector is not expected to expand in the future. Apparently, local development groups have not experienced great success in attracting new employers to the area. This is the result of two factors: (1) neighboring North Dakota has a very aggressive tax incentive program for new business and (2) the state of Montana is devoting its resources to developing industry in the eastern part of the state.

#### **CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA**

The bank's performance in meeting the credit needs in its assessment area is considered satisfactory. The following criteria were analyzed to determine this rating.

##### Loan-to-Deposit Ratio Analysis

The bank's loan-to-deposit ratio meets the standards for satisfactory performance. The bank's quarterly loan-to-deposit ratio is relatively low and has fluctuated between 41% and 50% since the bank became a state member bank on January 1, 1995. Based on the March 31, 1996, Uniform Bank Performance data, the bank's loan-to-deposit ratio does not compare favorably with its peer group. These data indicate that the bank's March 31, 1996, loan-to-deposit ratio of 41% ranks the bank in the 13th percentile in comparison with its peers. Based on the data for the six calendar quarters since January 1, 1995, the quarterly average of the bank's net loan-to-deposit ratio is 45%. The following chart summarizes the bank's loan-to-deposit ratio and its components since January 1, 1995.

DATE	NET LOANS (In thousands)	DEPOSITS (In thousands)	NET LOAN-TO- DEPOSIT RATIO
December 31, 1994	\$14,670	\$32,715	44%
March 31, 1995	\$14,240	\$32,328	43%
June 30, 1995	\$15,300	\$30,903	48%
September 30, 1995	\$15,845	\$30,996	50%
December 31, 1995	\$15,793	\$33,196	47%
March 31, 1996	\$14,829	\$35,287	41%

The bank's average loan-to-deposit ratio is below the quarterly average ratios of its local competitors. Based on quarterly ROC data, the following table identifies the asset size and quarterly average loan-to-deposit ratios for the bank and its competitors.

BANK	TOTAL ASSETS (March 31, 1996) (In thousands)	QUARTERLY AVERAGE LOAN-TO-DEPOSIT RATIO
Subject Bank	\$38,618	45%
Competitor A	\$29,527	64%
Competitor B	\$13,043	47%

In addition to the competitor banks listed above, several nonbank entities and one branch office of a Billings bank extend credit to residents of the bank's assessment area. The many financial institutions operating within the bank's assessment area create a very competitive credit market.

The bank's quarterly loan-to-deposit ratio is lower than that of its competitors for several reasons. As a result of a recent merger of another Plentywood bank with a financial institution headquartered in Billings, Montana, the bank has experienced a surge of new deposits. Consequently, the bank's deposits have increased 6% since January 1, 1996. In contrast, Competitors A and B have only experienced minimal deposit growth since the beginning of the year. In addition, the competitors listed above are located in communities other than Plentywood. These competitors are the only banks located in their respective communities.

Although low, the bank's loan-to-deposit ratio also reflects the lack of credit demand by residents of its assessment area. Credit demand is significantly influenced by the demographics of the local community. Approximately 48% of the assessment area's population is composed of persons who are 65 or older or younger than 18; members of these age brackets do not have significant credit needs. Additionally, the fact that local ranches and farms are typically passed from one family generation to the next limits demand for agricultural loans.

The bank has originated numerous commercial loans to businesses with gross annual revenues of less than \$1 million. Most of these businesses are the sole providers of their respective services or product lines within the assessment area. The bank's loan portfolio also includes a loan to build a five-unit housing complex in Plentywood. The housing complex specifically benefits low- and moderate-income residents of the assessment area.

Despite being low, the bank's loan-to-deposit ratio appears reasonable and meets the standards for satisfactory performance given demographic characteristics of its assessment area. It appears that the bank's lending activities are restricted by community demographic factors and market competition, and its loan-to-deposit ratio is not indicative of a lack of

willingness to extend credit to local residents and businesses or any unmet credit needs.

#### Lending in the Assessment Area

The bank's lending activity within its assessment area meets the standards for satisfactory performance. In the six months before the evaluation, the bank made a majority of its loans to residents of its assessment area. The table below shows the percentage of consumer and agriculture loans by total number and dollar amount originated within the assessment area.

PERCENTAGE OF LOANS IN THE ASSESSMENT AREA		
Loan Type	Total Number of Loans	Total Dollar Amount of Loans
Consumer	89%	82%
Agriculture	75%	73%

The data is based on a statistical sampling of consumer and agricultural loans originated in the six months before the evaluation. As the data indicate, the bank's lending activity is concentrated within the assessment area. Accordingly, the bank's lending meets this category's standard for satisfactory performance.

#### Lending to Borrowers of Different Income Levels and to Businesses of Different Sizes

The bank's level of lending to individuals of different incomes and to businesses of different sizes exceeds the standards for satisfactory performance. As discussed, the CRA classifies income levels into four categories: low income, moderate income, middle income, and upper income. The median household and family incomes for the bank's assessment area are \$20,728 and \$25,265, respectively. Both figures are below the statewide nonmetropolitan household and family incomes for the state of Montana.

The following table shows the percentage of consumer loans made to borrowers of different income levels.

DISTRIBUTION OF LOANS IN THE ASSESSMENT AREA BY BORROWER INCOME LEVELS*				
Loan Type	Low-Income Borrowers	Moderate-Income Borrowers	Middle-Income Borrowers	Upper-Income Borrowers
Consumer				
Total Number of Loans	43%	36%	11%	9%
Total Amount of Loans	56%	27%	9%	7%
*Income level is determined based on Montana's 1995 nonmetropolitan median family income of \$32,200.				

The data reveal that the bank extends a large percentage of its consumer loans to low- and moderate-income borrowers. Loans to these borrowers represented 79% of the total number of loans and 83% of the total amount of loans in the sample although low- and moderate-income households comprise 43% of the assessment area population. More specifically, low-income households represent 24% of the local population, and moderate-income households represent 19%. Thus, the bank's consumer lending to low- and moderate-income borrowers exceeds the representation of such persons in the assessment area. This concentration of consumer loans to members of both income categories is particularly commendable considering the demographic data.

Based on the loans sampled during the evaluation, the bank originates all its agricultural loans to small farms. In addition, almost all the sampled loans had loan amounts of \$100,000 or less. More specifically, 97% of the total number of agricultural loans to borrowers in the assessment area, representing 82% of the total amount of loans, had loan amounts of \$100,000 or less. The remaining 3% of the sampled agricultural loans had amounts greater than \$100,000 but less than or equal to \$250,000.

Based on the income distribution of the bank's borrowers and the demographics of the assessment area, the bank's level of lending to low- and moderate-income borrowers and small farms exceeds the standards for satisfactory performance.

#### Geographic Distribution of Loans

The distribution of the bank's loans throughout the assessment area meets the standards for satisfactory performance. As previously discussed, the bank's assessment area includes one moderate-income and two middle-income BNAs. The bank's main office is located in a middle-income BNA. The following table shows the distribution of the bank's consumer and agricultural loans in moderate- and middle-income BNAs.



DISTRIBUTION OF LOANS IN THE ASSESSMENT AREA BY BNA INCOME LEVEL*		
Loan Type	Moderate-Income BNA	Middle-Income BNA
<u>Consumer</u>		
Total Number of Loans	12%	88%
Total Amount of Loans	27%	73%
<u>Agriculture</u>		
Total Number of Loans	8%	92%
Total Amount of Loans	20%	80%
*The bank's assessment area does not include any low- or upper-income BNAs.		

The bank's consumer and agricultural lending performance in the moderate-income BNAs is reasonable considering the representation of residents in this BNA within the assessment area population. The total population of the moderate-income BNA is 945, which is 20% of the total assessment area population. Given this population distribution, the total dollar amount of consumer loan originations to residents of the moderate-income BNA exceeds expectations. Conversely, the total number of loans extended to consumers in the moderate-income BNA is somewhat lower than expected, based on population demographics. The bank's agricultural loan portfolio displays characteristics similar to the consumer loan portfolio. The dollar amount of agriculture loans meets expectations in light of the population demographics; however, the total number of agriculture loans extended to borrowers in the moderate-income BNA is somewhat lower than expected.

Based on these loan portfolio characteristics, it appears that the bank is willing to extend loans to borrowers in the moderate-income BNA. In fact, the amount of each origination to borrowers residing in the moderate-income BNA is relatively larger than that to borrowers from the middle-income BNAs. The fact that the bank has extended fewer loans to borrowers from the moderate-income BNA appears to reflect the bank's central location within its defined assessment area and the location of competitors. The moderate-income BNA, in the southern section of the assessment area, is served by a credit union in Medicine Lake, Montana, and a bank in Froid, which is located a few miles from Sheridan County's southern boundary. The bank's lending in the moderate-income BNA probably reflects the location of competitors in and near the southern section of the bank's assessment area.

Given these factors, the bank's lending activities in the moderate-income BNA meet the standards of satisfactory performance.

#### General Comments

The evaluation revealed a procedural violation of the technical aspects of the Fair Credit Reporting Act. Management promised prompt corrective action. In addition, the bank has not received any CRA complaints since January 1, 1995, the date it became a state member bank.

## **PUBLIC DISCLOSURE**

May 28, 1996  
Date of Evaluation

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## **COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION**

Montana State Bank  
Name of Depository Institution

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093008050000  
Identification Number of Institution

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Plentywood, Montana  
Address of Institution

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Federal Reserve Bank of Minneapolis  
250 Marquette Avenue  
Minneapolis, Minnesota 55401-2171

NOTE: This evaluation is not, nor should it be construed as, an assessment of the financial condition of this institution. The rating assigned to this institution does not represent an analysis, conclusion, or opinion of the federal financial supervisory agency concerning the safety and soundness of this financial institution.